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**Research Update:**

## Health Care Service Corp. Ratings Raised To 'AA-' From 'A+' On Strengthened Credit Risk Profile; Outlook Stable

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## Research Update:

# Health Care Service Corp. Ratings Raised To 'AA-' From 'A+' On Strengthened Credit Risk Profile; Outlook Stable

## Overview

- Health Care Service Corp.'s (HCSC) credit risk profile has strengthened in connection with sustained earnings improvement and business line development, among other capital growth factors.
- As a result, we are raising our ratings on HCSC and its subsidiary operations, Dearborn National.
- The stable outlook reflects our expectation that HCSC will sustain its leading presence in its core markets, maintain its balance-sheet strength, and achieve sustained, albeit lower, profitability.

## Rating Action

On Oct. 26, 2018, S&P Global Ratings raised its long-term financial strength and issuer credit ratings on Health Care Service Corp. (d/b/a Blue Cross Blue Shield of Illinois, New Mexico, Oklahoma, Texas and Montana) to 'AA-' from 'A+'. The outlook is stable.

At the same time, we raised our long-term issuer credit and financial strength ratings on HCSC's strategically important subsidiaries, Dearborn National Life Insurance Co. and Dearborn National Life Insurance Co. of New York (collectively, Dearborn National) to 'A+' from 'A'. The outlook is stable.

## Rationale

The upgrade reflects HCSC's improved operating performance and significantly strengthened capitalization, which we expect to persist through 2020. Recent above-trend operating performance for 2017-2018 stems from enhanced pricing flexibility, product redesign, and moderating underlying claims trends. Other contributing factors include favorable investment portfolio development and the benefits from the 2017 tax reform, which we expect to enhance HCSC's balance-sheet position through 2020. We also expect HCSC's balance-sheet position to remain a key rating strength as operating performance peaks for 2018 with an EBIT return on revenue (ROR) near 6%, moderating to a more-sustainable run-rate and for capitalization to continue to reflect material 'AAA' redundancy in the next two years.

## Outlook

The stable outlook reflects our expectation that HCSC will maintain its leading market position in its core markets and maintain its meaningfully improved balance-sheet strength and strong liquidity position in the next two years. During this time, we expect modest single-digit enrollment and revenue growth with moderating underlying pretax EBIT ROR of 3%-4%, which is more in-line with our run-rate expectations for larger not-for-profit Blue branded peers.

### Downside scenario

We may lower our ratings by one notch in the next 24 months if HCSC underperforms relative to our current operating performance expectations. Meaningful erosion in performance could indicate the company is unable to gain traction with its strategic initiatives for its government-program segments. We do not expect HCSC's capital adequacy to fall below 'AAA' given its already very high present level.

### Upside scenario

Although unlikely, we could raise our ratings by one notch in the next 24 months if HCSC maintains its balance-sheet strength and historically strong operating performance while reflecting a more-diversified geographic and product scope. This could boost earnings quality and further lower the capital volatility risk inherent in its credit profile.

## Related Criteria

- Criteria - Insurance - General: Methodology For Assessing Capital Charges For U.S. RMBS And CMBS Securities Held By Insurance Companies, Aug. 29, 2014
- Criteria - Insurance - General: Enterprise Risk Management, May 7, 2013
- Criteria - Insurance - General: Insurers: Rating Methodology, May 7, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Criteria - Insurance - General: Methodology For Assessing Capital Charges For Commercial Mortgage Loans Held By U.S. Insurance Companies, May 31, 2012
- Criteria - Insurance - General: Methodology For Calculating The Convexity Risk In U.S. Insurance Risk-Based Capital Model, April 27, 2011
- Criteria - Insurance - General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

- Criteria - Insurance - Life: Liquidity Model For U.S. And Canadian Life Insurers, April 22, 2004

## Ratings List

Upgraded; Outlook Action

	To	From
Health Care Service Corp. d/b/a Blue Cross Blue Shield of Illinois, New Mexico, Oklahoma, Texas and Montana		
Issuer Credit Rating		
Local Currency	AA-/Stable/--	A+/Positive/--
Financial Strength Rating		
Local Currency	AA-/Stable/--	A+/Positive/--
Dearborn National Life Insurance Co.		
Dearborn National Life Insurance Co. of New York		
Issuer Credit Rating		
Local Currency	A+/Stable/--	A/Positive/--
Financial Strength Rating		
Local Currency	A+/Stable/--	A/Positive/--

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